

**PRESENTATION/CASE STUDY
DETERMINATION OF MAJOR FEDERAL PROGRAM
ON OMB CIRCULAR A-133 AUDITS
PRESENTED AT 14TH ANNUAL AICPA
NATIONAL GOVERNMENTAL ACCOUNTING &
AUDITING UPDATE CONFERENCE**

MAJOR PROGRAM DETERMINATION

Steps of Risk-Based Approach — Step 1

- Identify Type A programs based on total Federal Awards (FA) expended:
 - Expenditures \$300k to \$10 mil - \$300k Expenditures
 - \$10 mil to \$100 mil - 3.0% of FA Expenditures
 - \$100 mil to \$1 bil - \$3 mil Expenditures
 - \$1 bil to \$10 bil - 0.30% of FA
 - Expenditures \$10 bil to \$20 bil - \$30 mil
 - Expenditures greater than \$20 bil - 0.15% of FA
- All other programs are labeled Type B
- Exclude large Type A loan programs from calculation
- Biennial audits: use total FA expended in two-year period

Steps of Risk-Based Approach — Step 2

- Identify *low-risk* Type A programs
 - Audited as a major program in 1 of 2 most recent years
 - In most recent year, no audit findings that are:
 - ◆ Reportable conditions in internal control
 - ◆ Material noncompliance with laws & regulations
 - ◆ Known questioned costs > \$10,000
 - ◆ Known questioned costs when likely questioned costs > \$10,000
 - ◆ Known fraud
 - ◆ Misrepresentations by auditee in summary schedule of prior audit findings
 - Use auditor judgment and criteria for Federal program risk provided in section _____.525 of Circular A-133
- Certain Type A programs may not be considered low-risk

Steps of Risk-Based Approach — Step 3

- Identify *high-risk* Type B programs
 - Use auditor judgment and criteria for Federal program risk provided in section _____.525 of Circular A-133
 - Risk assessments are not needed for small Type B programs (generally, programs under \$100k)

Criteria for Federal Program Risk -- Section .525 of Circular A-133

(to be used in Steps 2 and 3)

■ Current and prior audit experience:

- Weaknesses in controls over Federal awards
- Multiple operating units administering program
- Significant subrecipients
- Complexity of EDP systems (new or recently changed)
- Prior audit findings
- No recent audit

■ Oversight by Federal agencies and pass-throughs (agency may identify programs at higher risk in compliance supplement, e.g., Medicaid)

■ Inherent risk (program complexity, phase in life cycle, materiality)

Steps of Risk-Based Approach — Step 4

■ Determine major programs as:

- All Type A programs, except low-risk Type A programs, plus
- High-risk Type B programs – using either of 2 options:
 - ◆ Option 1: At least 1/2 of high-risk Type B programs but not to exceed the number of low-risk Type A programs (the “cap”) or
 - ◆ Option 2: One high-risk Type B program for each low-risk Type A program, plus
- Any programs required to be audited as major by grantor (grantor must notify 180 days before year-end and agree to pay full incremental cost -- Example: Federal Family Education Loan program -- Guaranty Agencies -- CFDA No. 84.032), plus
- Any Type A or B programs to meet percentage of coverage rule

Percentage of Coverage Rule

- The sum of major program expenditures must encompass at least 50% of the auditee’s total Federal awards expended
- If auditee qualifies as a “low-risk auditee” under section _____.530 of the Circular, then percentage of coverage is reduced to 25%
- Percentage of coverage rule must be met even if “the cap” on the number of major programs is exceeded
- Percentage of coverage rule is applied after Steps 1, 2, 3, and all other parts of Step 4 are performed
- When selecting additional programs to audit as major to comply with percentage of coverage rule, not necessary to consider risk -- only \$

Low-Risk Auditee Criteria -- Section .530 of Circular A-133

(to be used in Step 4, under the percentage of coverage rule)

Auditee must meet all criteria for last two years

- Annual audits in accordance with A-133 (or A-128, as applicable)
- Unqualified opinion on FS and SEFA (cog. may waive)
- No material weaknesses in internal control (cog. may waive)
- No Type A programs had:
 - Material weaknesses in internal control
 - Material noncompliance
 - Known or likely questioned costs > 5% of a Type A program

Deviation from Use of Risk Criteria -- .520(i) of Circular A-133

- For 1st year audits, major programs may be determined as:
 - All Type A programs, plus
 - Any Type B programs necessary to meet the percentage of coverage rule
- “1st year audit” defined as the 1st year:
 - Entity is audited under the Revised Circular A-133, published 6/30/97
 - Under a change in auditors (can be used only once every 3 years)

Risk-Based Approach -- An Overview

- Objective: Rotate the mix of Federal awards covered by audit over time
- Auditors are responsible for determining major programs using risk-based approach
- May delay use of risk-based approach in 1st year under revised A-133
- Auditors’ judgment required and presumed correct, if properly documented
- Incorporates percentage of coverage rule and low-risk auditee concept
- A-133 prescribes a 4-step process to implement risk-based approach

RISK-BASED APPROACH FOR DETERMINING MAJOR PROGRAMS EXAMPLE FOR XYZ CASE STUDY

Introduction

The final revision to OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations,” published June 30, 1997, requires that the auditor use a risk-based approach in determining major programs. Sections of the Circular that describe the requirements of the risk-based approach are:

§.520 Major program determination

§.525 Criteria for Federal program risk

§.530 Criteria for a low-risk auditee

References in this example which are preceded by “§___.” are to the section numbers of OMB Circular A-133.

Also, to mitigate any implementation problems with the risk-based approach, the provision for deviation from use of risk criteria provided in §. 520(I) applies to the first year this Circular is applicable and permits auditors to defer implementation of the risk-based approach for one year (i.e., the risk-based approach is optional for audits of fiscal years ending June 30, 1997).

The following example for XYZ, a municipality, is intended to illustrate the application of the risk-based approach over a four year period (1997 through 2000). Included with the example are worksheets titled “Major Program Determination Worksheet for XYZ” and “Summary of Audit Results for XYZ.” (Note: These worksheets are training tools only and are not required by OMB Circular A-133.)

Background on XYZ

XYZ had the following of Federal awards expended for the year ended June 30, 1997:

Program 1	\$ 2,600,000
Program 2	2,200,000
Program 3	2,600,000
Program 4	2,000,000
Program 5	270,000
Program 6	240,000
Program 7	90,000
Total	<u>\$10,000,000</u>

For purposes of this example, the programs and the amount of Federal awards expended for XYZ are the same in 1997, 1998, 1999, and 2000.

XYZ's fiscal year ends on June 30. For simplicity, the year ending June 30, 1996, will be referred to as 1996, the year ending June 30, 1997, as 1997, etc. XYZ had an audit conducted in accordance with OMB Circular A-128 since 1991.

None of the Federal programs are material to XYZ's financial statements. For each year, the opinion on the general purpose financial statements is unqualified and the auditor's reports did not include any reportable conditions or material instances of noncompliance at the financial statement level.

Program 1 Most of the expenditures from Program 1 are for payroll expenses. Employees paid from this program spend all of their time working on this program. XYZ has historically had an accurate and well controlled payroll system. No significant changes occurred in the payroll system or its personnel in the last several years. This program was audited for each of the last several years as a major program. No reportable conditions, material matters of noncompliance, or other audit findings were reported in the last several years.

Program 2 This program has complex eligibility requirements. Audits of the last three years have disclosed matters of noncompliance, numerous reportable conditions, and questioned costs. In 1996, there was an opinion qualification for a material noncompliance.

Program 3 This program is similar to Program 1 and was audited for the last several years as a major program. No reportable conditions, material matters of noncompliance, or other audit findings were reported in the last several years.

Program 4 This is a new program in 1997, and it is similar to Program 1. This program was not audited previously.

Program 5 This program is administered 100% by a district office of XYZ which is located several hundred miles away from the city's main office. The district office is staffed by a office manager and a part-time clerical employee with limited training. Program expenditures are approved by the office manager and, to minimize disruption, the original supporting documentation is retained at the district office. Because of the complexity of compliance requirements and the relatively small size of this program, the central office's involvement is minimal. In previous audits, Program 5 was not audited as a major program or used to comply with the 50 percent rule. Accordingly, controls were not subjected to risk assessment or testing and tests of compliance were not performed.

Program 6 This program was not previously audited as a major program or used to comply with the 50 percent rule. However, in 1996 a monitoring team from the Federal awarding agency performed a review and found significant internal control and compliance problems.

Program 7 This program is administered at the same district office as Program 5 and, due to its small size, it was not considered a major program or used to comply with the 50 percent rule in previous audits.

Analysis for Major Program Determination in 1997

Step 1 - Identify Type A and Type B Programs

Since XYZ receives less than \$100 million, a Type A program is determined to be any Federal program with Federal awards expended exceeding the larger of \$300,000 or 3% of total Federal expenditures (3% X \$10,000,000 = \$300,000). In this example, any program with Federal expenditures exceeding \$300,000 is a Type A program and any program at or below \$300,000 is a Type B program. (§ .520(b)(1))

Programs 1, 2, 3, and 4 are Type A and Programs 5, 6, and 7 are Type B. This will be the same for all years since, in this example, the amount of Federal awards expended are the same for each year.

	<u>\$</u>	<u>Type</u>
Program 1	\$ 2,600,000	A
Program 2	2,200,000	A
Program 3	2,600,000	A
Program 4	2,000,000	A
Program 5	270,000	B
Program 6	240,000	B
Program 7	<u>90,000</u>	B
Total	<u>\$10,000,000</u>	

Step 2 - Identify Low-risk Type A Programs

Programs 1 and 3 are identified as low-risk because the programs were audited as major programs in 1996 with no audit findings, there were no significant changes in the personnel or systems affecting the programs which increased risk, and, in the auditor's judgment, the programs are low-risk due to the non-complex nature of the programs.

Program 2 is not low-risk because of audit findings in the prior year and Program 4 is not low-risk because it is a new program and was not audited previously.

Step 3 - Identify High-risk Type B Programs

Before risk assessments are begun, the auditor should consider which option is likely to be used to select high-risk Type B programs as major programs, if any. In this case, Option 1 is assumed to be the most efficient approach for this and all years of the example. Therefore, risk assessments are performed for programs 5 and 6.

A risk assessment is not performed on Program 7 because § .520(d)(2) of the Circular permits the auditor to exclude relatively small Federal programs from the risk analysis. For XYZ, risk assessments are not required for programs below \$100,000.

Programs 5 and 6 are identified as high-risk.

Criteria considered in identifying Program 5 as high-risk include dollar size, the program was never audited before, complexity of the program, and concern over control risk due to limited oversight of the district office by headquarters and lack of separation of duties and training related to district office staff.

Program 6 was identified as high-risk because of its size, it was never audited before, and the concerns raised by the 1996 monitoring visit. The auditor was told by the management of XYZ that the internal control concerns raised during the 1996 monitoring visit were not corrected. However, XYZ appointed a committee to start working on the internal control concerns and management assured the auditor that corrective action is imminent.

	1997		
	\$	<u>Type</u>	<u>Risk</u>
Program 1	\$ 2,600,000	A	Low
Program 2	2,200,000	A	High
Program 3	2,600,000	A	Low
Program 4	2,000,000	A	High
Program 5	270,000	B	High
Program 6	240,000	B	High
Program 7	<u>90,000</u>	B	-----
Total	<u>\$10,000,000</u>		

Step 4 - Determine Major Programs

Part 1

Non Low-risk Type A Programs - Type A Programs 2 and 4 are not low-risk and, therefore, are major programs.

Part 2

High-risk Type B Programs - § .520(e)(2)(I)(A) requires that at least one-half of the high-risk Type B programs be audited as major programs. However, that Section establishes a cap that the number of high-risk Type B programs audited as major programs need not exceed the number of low-risk Type A programs.

Programs 5 and 6 are identified as high-risk Type B programs under Step 3. Therefore, one-half of the number of high-risk Type B programs is one. Since the number of low-risk Type A programs (i.e., Programs 1 and 3) is two, the cap is not applicable in this case. Therefore, the auditor is required to select one high-risk Type B program as a major program. The auditor may choose either Program 5 or 6 and is not required to justify a decision of which high-risk Type B program is audited as a major program. The auditor selects Program 5 in this example. (Note: If there were no low-risk Type A programs, the auditor would not be required to audit any high-risk Type B programs as major programs. In addition, the auditor would not be required to perform risk assessments of Type B programs if there were no low-risk Type A programs.)

Part 3

Percentage of Coverage Rule - Aggregate Federal expenditures for major Programs 2, 4, and 5, total \$4,470,000. This is only 44.7% of total Federal awards expended.

Low-risk Auditee Determination - XYZ does not qualify as a low-risk auditee (See §530 for criteria of a low-risk auditee) because there was material noncompliance in a Type A program (Program 2) during one of the preceding two years (1996). Therefore, the single audit must cover at least 50% of total Federal expenditures to comply with the 50 percent rule.

To achieve 50% coverage, the auditor chooses to audit Program 1, a low-risk Type A program, as a major program. This provides coverage over \$7,070,000 or 70.7% of Federal awards expended, which meets the 50 percent rule. (Note: The auditor could have selected any other Federal programs to meet this 50 percent rule.)

% of Coverage Rule

$$\begin{array}{rcl} & \textbf{HIGH} & \\ \$10,000,000 & \times .50 & = \$5,000,000 \end{array}$$

$$\begin{array}{rcl} & \textbf{LOW} & \\ \$10,000,000 & \times .25 & = \$2,500,000 \end{array}$$

**1997
Major Programs**

High Risk	\$
Program 2	\$2,200,000
Program 4	\$2,000,000
Program 5	<u>\$ 270,000</u>
	\$4,470,000 (44.7% of \$10,000,000)

% of Coverage Rule

Program 1	<u>\$2,600,000</u> (26% of \$10,000,000)
Total	<u>\$7,070,000</u> (70.7% of \$10,000,000)

Results of 1997 Audit

Audit

Program 1 - No audit findings.

Program 2 - Internal controls improved. However, there was one reportable condition in internal controls. There were three audit findings related to noncompliance and known questioned costs of \$50,000. In evaluating the effect of questioned costs on the opinion on compliance, the auditor's best estimate was that total questioned costs did not exceed 3% of Program 2 expenditures. In the auditor's judgement, there was not material noncompliance.

Program 4- No audit findings.

Program 5 - Significant problems were discovered at the district office. The district office manager had neither retained documentation to support the expenditures nor documentation to support compliance with the program's complex requirements. All costs of the program were questioned, and there were material weaknesses in internal control and material matters of noncompliance.

Follow-up - Program 2 was the only program with prior audit findings and the follow-up was performed as part of auditing this program as a major program in the current year. For purposes of this example, in any year a program is major, the follow-up will be assumed to be done as part of auditing the major program. For non-major programs, audit follow-up is listed separately in the results of audit section.

Analysis for Major Program Determination in 1998

Step 1 - Identify Type A and Type B Programs

Programs 1, 2, 3, and 4 are Type A and Programs 5, 6, and 7 are Type B.

Step 2- Identify Low-risk Type A Programs

Programs 1, 3, and 4 are identified as low-risk because the programs were audited in one of the last two years with no audit findings and there are no other indications of risk greater than low.

Program 2 is not low-risk because the 1997 audit disclosed a reportable condition in internal control and significant questioned costs.

Step 3 - Identify High-risk Type B Programs

Programs 5 and 6 are identified as high-risk for the same reasons as in 1997. In addition, the 1997 audit disclosed material weaknesses in internal control and material matters of noncompliance for Program 5.

	1998		
	\$	<u>Type</u>	<u>Risk</u>
Program 1	\$ 2,600,000	A	Low
Program 2	2,200,000	A	High
Program 3	2,600,000	A	Low
Program 4	2,000,000	A	Low
Program 5	270,000	B	High
Program 6	240,000	B	High
Program 7	<u>90,000</u>	B	-----
Total	<u>\$10,000,000</u>		

Step 4 - Determine Major Programs

Part 1

Non Low-risk Type A Programs - Type A Program 2 is not low-risk and, therefore, is a major program

Part 2

High-risk Type B Programs - In accordance with § .520(e)(2)(I) (A), the auditor is required to audit one high-risk Type B program. (One-half of the high-risk Type B programs is one, and the cap does not apply since the number of low-risk Type A programs is three.)

The auditor selects Program 6 based upon the following analysis. Most of the 1998 activity in Program 5 occurred before a new district manager was hired and the auditor concludes it would be of little value to audit this program until management has time to fix the known problems. Also, Program 6 was never audited before and auditing this program as a major program will determine whether corrective action has occurred for the problems disclosed by the 1996 monitoring visit. The management of XYZ is supportive of this because the Federal awarding agency has scheduled a monitoring visit of Program 6 in 1999 and management wants to ensure that Program 6 is in order. (Note: Under the risk-based

approach it would be permissible for the auditor to select Program 5 as a major program. The auditor is not required to justify a decision of which high-risk Type B program is audited as a major program.)

Part 3

Percentage of Coverage Rule - Aggregate Federal expenditures for major Programs 2 and 6 are \$2,440,000, or 24.4% of total Federal awards expended.

Low-risk Auditee Determination - XYZ does not qualify as a low-risk auditee because there was material noncompliance in a Type A program (Program 2) during one of the preceding two years (1996). Therefore, the single audit must cover at least 50% of total Federal expenditures to comply with the 50 percent rule.

To achieve 50% coverage, the auditor chooses to audit Program 3. This provides coverage of Federal awards expended totaling \$5,040,000 or 50.4% which meets the 50 percent rule. (Note: The auditor could select other Federal programs to comply with the 50 percent rule.)

1998 Major Programs	
High Risk	\$
Program 2	\$2,200,000
Program 6	<u>\$ 240,000</u>
	\$4,440,000 (24.4% of \$10,000,000)
<u>% of Coverage Rule</u>	
Program 3	<u>\$2,600,000</u> (26% of \$10,000,000)
Total	<u>\$5,040,000</u> (50.4% of \$10,000,000)

Results of 1998 Audit

Audit

Program 2 - There has continued to be improvement in both internal controls and compliance for this program. No reportable conditions were reported. However, there were known questioned costs of \$35,000. In evaluating the effect of questioned costs on the opinion on compliance, the auditor's best estimate was that total questioned costs did not exceed 2% of Program 2 expenditures. In the auditor's judgment, there was not material noncompliance.

Program 3 - No audit findings.

Program 6 - Some improvements were made in this program since the 1996 monitoring visit. However, the auditor reported a reportable condition in internal controls, material matters of noncompliance, and known questioned costs totaling \$24,000.

Audit Follow-up

Program 5 - In response to the problems found in 1997 for Program 5, corrective action was initiated. XYZ replaced the district manager in May 1998. The qualifications of the new district manager indicate that this person is knowledgeable in the program's compliance requirements. The new district manager scheduled extensive training for the part-time employee. Also, headquarters just started monitoring the district office by reviewing all transactions and otherwise supervising district activity. XYZ is also negotiating with the Federal awarding agency concerning pay-back of the questioned costs. (Note: In accordance with § .500(e), the auditor is required to perform audit follow-up procedures on Program 5 in 1998 even though it was not a major program in that year.)

Analysis for Major Program Determination in 1999

Step 1 - Identify Type A and Type B Programs

Programs 1, 2, 3, and 4 are Type A and Programs 5, 6, and 7 are Type B.

Step 2 - Identify Low-risk Type A Programs

Programs 1, 3, 4 are identified as low-risk because the programs were audited in one of the last two years with no audit findings and there are no other indications of risk greater than low.

Program 2 is not low-risk because of significant questioned costs in 1998.

Step 3 - Identify High-Risk Type B Programs

Programs 5 and 6 are identified as high-risk. In the auditor's judgment, Program 5 is still considered high-risk because of severity of the problems disclosed in the 1997 audit and that corrective action was not completed. Also, Program 6 is considered high-risk because of the audit findings in the 1998 audit.

	1999		
	\$	<u>Type</u>	<u>Risk</u>
Program 1	\$ 2,600,000	A	Low
Program 2	2,200,000	A	High
Program 3	2,600,000	A	Low
Program 4	2,000,000	A	Low
Program 5	270,000	B	High
Program 6	240,000	B	High
Program 7	<u>90,000</u>	B	-----
Total	<u>\$10,000,000</u>		

Step 4 - Determine Major Programs

Part 1 - Non Low-risk Type A Programs - Type A Program 2 is not low-risk and therefore is a major program.

Part 2 - High-Risk Type B Programs - In accordance with § .520(e)(2)(I)(A), the auditor is required to audit one high-risk Type B program. (One-half of the high-risk Type B programs is one, and the cap does not apply since the number of low-risk Type A programs is three).

The auditor selects Program 5 to audit as a major program in order to follow-up on the district office activity.

Part 3

Percentage of Coverage Rule - Aggregate Federal expenditures for major Programs 2 and 5 are \$2,470,000 or 24.7% of total Federal awards expended.

Low-risk Auditee Determination - XYZ qualifies as a low-risk auditee. During the preceding two years

(1997 and 1998), XYZ was audited under Circular A-133, the opinions on XYZ 's financial statements were unqualified, and no material weaknesses in internal controls at the financial statement level were reported. Also, the only Type A program with audit findings was Program 2, and these findings were not material weaknesses in internal controls, material noncompliance to the program, or known or likely questioned costs which exceeded 5% of the total expenditures for Program 2. Therefore, under criteria for a low-risk auditee, XYZ only needs to cover 25% of Federal expenditures. (Note: Even though there was material noncompliance in Program 6, a major program in 1998, this does not preclude the auditee from qualifying as a low-risk auditee, since Program 6 is a Type B program. The criteria for low-risk auditee in §. 53 0(d) only applies to Type A programs.)

To achieve 25% coverage, the auditor chooses to audit Program 7. Program 7 was never audited as a major program and is handled by the same district office as Program 5. Also, the management of XYZ expressed interest in having the total activities of the district office audited to ensure that all prior problems were corrected by the new district manager. Even though Program 7 (as a relatively small Federal program with expenditures less than \$100,000 as provided by § .525(d)(2)) was not required to be included in the risk-analysis, the auditor may choose it as a major program to meet the 25% requirement for a low-risk auditee.

1999 Major Programs	
High Risk	\$
Program 2	\$2,200,000
Program 5	<u>\$ 270,000</u>
	\$4,470,000 (24.7% of \$10,000,000)
<u>% of Coverage Rule</u>	
Program 7	<u>\$ 90,000</u> (.9% of \$10,000,000)
Total	<u>\$5,040,000</u> (25.6% of \$10,000,000)

Results of 1999 Audit Audit

Program 2 - Again, there continued to be improvements in the internal controls over this program. No reportable conditions were reported. There was only one audit finding with questioned costs of \$10,200. The cause of this questioned cost was that the two employees who usually handle this area happened to be out sick on the same day, and the department supervisor filled in and botched the transaction. In the auditor's judgment, there was not material noncompliance.

Program 5 and Program 7-

No audit findings. The new district manager and assistant were properly administering these programs and headquarters was continuing to monitor the activity. Corrective action was complete on all prior findings for Program 5.

Audit Follow-up

Program 6 - Corrective action was not completed on the conditions surrounding the reportable condition disclosed in the 1998 audit.

Analysis for Major Program Determination in 2000

Step 1- Identify Type A and Type B Programs

Programs 1,2,3, and 4 are Type A and Programs 5,6, and 7 are Type B.

Step 2- Identify Low-risk Type A Programs

Programs 2 and 3 are identified as low-risk because the programs were audited in one of the last two years and there are no indications of risk greater than low. Even though Program 2 had an audit finding for questioned costs greater than \$10,000 in 1999, in the auditor's judgment this does not preclude the program from being low-risk because the 1999 questioned cost is less than one half of one percent of the program's total expenditures and the cause of the questioned cost is isolated.

Programs 1 and 4 are not low-risk because these programs were not audited as major programs in either of the last two years.

Step 3 - Identify High-Risk Type B Programs

In the auditor's judgment, Program 6 is considered high-risk because of the severity of the problems disclosed in the 1998 audit.

	2000		
	\$	<u>Type</u>	<u>Risk</u>
Program 1	\$ 2,600,000	A	High
Program 2	2,200,000	A	Low
Program 3	2,600,000	A	Low
Program 4	2,000,000	A	High
Program 5	270,000	B	Low
Program 6	240,000	B	High
Program 7	90,000	B	-----
Total	<u>\$10,000,000</u>		

Step 4 - Determine Major Programs

Part 1

Non Low-risk Type A Programs - Type A Programs 1 and 4 are not low-risk and, therefore, are major programs.

Part 2

High-Risk Type B Programs - In accordance with § .520(e)(2)(I)(A), the auditor is required to audit one high-risk Type B program. Since there is only one high-risk Type B program, the auditor must audit it in order to achieve coverage of at least one-half. The cap does not apply since the number of low-risk Type A programs is two.

Since Program 6 is the only high-risk Type B program, it is audited as a major program.

Part 3

Percentage of Coverage Rule - Aggregate Federal expenditures for major Programs 1,4, and 6 are \$4,840,000, or 48.4% of total Federal awards expended.

Low-risk Auditee Determination - XYZ continues to qualify as a low-risk auditee. During the last two years (1998 and 1999), XYZ was audited under Circular A-133, the opinions on XYZ 's financial statements were unqualified, and no material weaknesses in internal controls at the financial statement level were reported.

Also, the only Type A program with audit findings was Program 2, and these findings were not material weaknesses in internal controls, material noncompliance to the program, or known or likely questioned costs which exceeded 5% of total expenditures for Program 2. Therefore, under criteria for a low-risk auditee, XYZ only needs to cover 25% of Federal expenditures.

The requirement for 25% coverage is met without selecting additional programs.

2000	
<u>Major Programs</u>	
High Risk	\$
Program 1	\$2,600,000
Program 4	\$2,000,000
Program 6	<u>\$ 240,000</u>
	\$4,840,000 (48.4% of \$10,000,000)
 <u>% of Coverage Rule</u>	
Not Applicable	
 Total	 <u>\$4,840,000</u> (48.8% of \$10,000,000)

Major Program Determination Worksheet for XYZ

		1997			1998			1999			2000		
Federal Expenditures		Step 4 Determination		Total	Step 4 Determination		Total Major	Step 4 Determination		Total	Step 4 Determination		Total Major
Type A		Part 1	Part 3		Part 1	Part 3		Part 1	Part 3		Part 1	Part 3	
1	\$2,600,000		26.0%	26.0%							26.0%		26.0%
2	\$2,200,000	22.0%		22.0%	22.0%		22.0%	22.0%		22.0%			
3	\$2,600,000					26.0%	26.0%						
4	\$2,000,000	20.0%		20.0%							20.0%		20.0%
Type B		Part 2			Part 2			Part 2			Part 2		
5	\$270,000	2.7%		2.7%				2.7%		2.7%			
6	\$240,000				2.4%		2.4%				2.4%		2.4%
7	\$90,000								0.9%	0.9%			
Total	\$10,000,000	44.7%	26.0%	70.7%	24.4%	26.0%	50.4%	24.7%	0.9%	25.6%	48.4%		48.4%
Qualify as low-risk auditee?		No			No			Yes			Yes		

Note - Step 4 of the risk-based approach consists of three distinct parts as follows:

Part 1 represents non low-risk Type A programs that are audited as major programs.

Part 2 represents high-risk Type B programs that are audited as major programs.

Part 3 represents additional programs that are audited as major programs to meet the percentage of coverage rule (50 percent for high-risk auditee and 25 percent for low-risk auditee)

Note - This worksheet is a training tool only and is not required by OMB Circular A-133.

SUMMARY OF AUDIT RESULTS for XYZ

Program	1996	1997	1998	1999
1	No audit findings	No audit findings		
2	Opinion qualification for material noncompliance.	One reportable condition in internal control. Three audit findings related to noncompliance and known questioned costs of \$50,000. Estimate of total questioned costs less than 3%. No material noncompliance.	Improvements in internal controls and compliance. No reportable conditions reported. Known questioned costs of \$35,000. Estimate of total questioned costs less than 2%. No material noncompliance.	Improvements in internal controls and compliance. No reportable conditions reported. One audit finding with questioned costs of \$10,200 which was an isolated instance. No material noncompliance.
3	No audit findings.		No audit findings.	
4		No audit findings.		
5		Significant problems discovered at district office. All program costs are questioned. Material weaknesses in internal control and material noncompliance.	<u>Audit Follow-up Only</u> Corrective action had been initiated. XYZ is negotiating with Federal awarding agency on pay-back of questioned costs.	No audit findings.
6			A reportable condition in internal controls, material matters of noncompliance, and known questioned costs totaling \$24,000.	<u>Audit Follow-up Only</u> Corrective action not completed on conditions surrounding reportable condition disclosed in the 1998 audit.
7				No audit findings.

Note: ●Shaded cell indicates program was not audited as a major program and audit follow-up was not required.

●This worksheet is a training tool only and is not required by OMB Circular A-133.

Factors to Consider in Performing Risk Analysis/Determining Major Federal Programs

Audit efficiency

Responsiveness to client requests

Severity of high risk assessment - i.e. number of factors considered

Rotation of programs audited

Auditor judgment